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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1937.

No. [redacted] 53

In the Matter of
TAX SERVICE ASSOCIATION OF ILLINOIS,
Alleged Bankrupt.

ROY G. HARRIS and BENJAMIN F. J. ODELL,
Petitioners,

vs.

AVERY BRUNDAGE COMPANY, et al., and DAHL-STEDMAN CO., et al.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

BENJAMIN F. J. ODELL,
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PETITION.

Roy G. Harris and Benjamin F. J. Odell, respondents o an intervening petition of Dahl-Stedman Co., et al., léd in the matter of Tax Service Association of Illinois, lleged bankrupt, through their counsel, pray that a writ

of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Seventh Circuit, entered in the above cause on March 9, 1938, affirming the decision of the District Court of the United States for the Northern District of Illinois, Eastern Division.

STATEMENT OF MATTER INVOLVED.

This is an appeal from orders of the District Court in an attempted bankruptcy proceeding, resisted by alleged bankrupt as a non-profit organization. The order directed that the sum of $48,580, out of a $72,000 escrow fund in the hands of three persons, be turned over to interveners, an alleged committee (appellees).

Various trade associations, on April 9, 1935, entered into an agreement (Rec. 24) with the Tax Service Association of Illinois, the alleged bankrupt, by which the latter agreed to attempt to persuade the Department of Finance of the State of Illinois to change its ruling in connection with the Illinois Retailers' Occupation Tax, commonly known as the Sales Tax. The alleged bankrupt, in accordance with said agreement, was paid $1500 in advance and was to receive not to exceed $20,000 if the Supreme Court of Illinois decided the Sales Tax question favorably. The alleged bankrupt agreed to retain attorney Benjamin F. J. Odell, one of the appellants and petitioners here, to act for and on behalf of the "subscribers" who were the various trade associations. Subsequently numerous contractors, by separate written contracts of various forms (Appendix *infra*) separately engaged appellant Odell (Rec. 169-170) to represent them in litigation over the extent of their liability as building contractors with respect to the so-called Sales Tax.

Pending determination of this legal issue, it was de-

cided to escrow their taxes as they accumulated. On May 2, 1935, Harris and Odell, petitioners here, together with E. M. Craig, the three escrowees, directed a letter to the National Builders Bank of Chicago, calling the attention of the bank to the opening of an account for the contractors in said bank entitled Sales Tax Escrow Fund. (Rec. 27.) The letter stated that the funds were in the custody and control of these three persons pending the outcome of proposed negotiations with the Department of Finance of the State of Illinois, and the letter contained directions that the funds were to be paid out only on signatures of the three escrowees whose signatures appeared on the letter, or their alternates.

The identity and relations of the escrowees have become significant. E. M. Craig was the secretary of the said various trade associations and in no way connected with the alleged bankrupt. Odell was the contractors' attorney. R. G. Harris was a vice president of the alleged bankrupt.

Negotiations with the Department of Finance being unsuccessful, the contractors, through their attorney Odell, instituted a suit in the Circuit Court of Cook County for the purpose of obtaining a construction of the said Tax Act. This bill filed by the contractors, was dismissed for want of equity. The contractors then appealed to the Supreme Court of the State of Illinois. The Supreme Court deciding in their favor, reversed the decision of the Circuit Court of Cook County and remanded the cause. (Rec. 51, *Blome Co.* v. *Ames*, 365 Ill. 456, 459.) In conformity with the decision of the Supreme Court, the Department of Finance of the State of Illinois was compelled to change its ruling and extend unqualified exemption from the Sales Tax on labor furnished by contractors, which it had not conceded theretofore. (Rec. 161.)

Subsequently, the Supreme Court voluntarily modified its said decision (Rec. 163, *Herlihy Mid-Continent Co. v. Nudelman*, 367 Ill. 600, 605) and instructed that the contractors were not liable for Sales Taxes on either labor or materials but completely exempt therefrom. As a result of the efforts of Odell, their attorney, the contractors are now exempt from the tax and entitled to refunds from the State of Illinois, estimated at hundreds of thousands of dollars.

On May 3, 1937, an involuntary petition in bankruptcy was filed against the Tax Service Association of Illinois; the said association resisted the petition upon the ground that it was a "not for profit corporation," and that the court had no jurisdiction to entertain an involuntary petition because it was not a "moneyed, business, or commercial corporation" within the purview of the Bankruptcy Act; (Rec. 77), denied it was insolvent, denied that it had committed any acts of bankruptcy, denied that there were sufficient creditors. Up until the time of decision of this case in the Circuit Court of Appeals, there had been no adjudication.

On May 24, 1937, there was in excess of $314,000 in the said escrow fund, and at that time said interveners filed an intervening petition in the Bankruptcy Court, making the three escrowees, the alleged bankrupt, the bankruptcy receiver and the bank, respondents, (Rec. 18) alleging that said money belonged to them and requested its return, and that none of the money belonged to the alleged bankrupt and asking that the three escrowees be compelled to sign a check turning over the funds and that the bank be compelled to honor the check.

Immediately after the filing of the said intervening petition, it became imperative to turn over 75 per cent of

the escrow fund to the Department of Finance of Illinois in order to avoid impending heavy penalties to the contractors. (Subsequently this amount was held not due as a tax.) For this purpose, an "agreed" order was entered May 27, 1937 turning over 75 per cent of the said money in the escrow fund to the Department of Finance of the State of Illinois. (Rec. 39.) In said order appellants were given until June 3, 1937 to file their answers or other pleadings to appellees' intervening petition, and appellants as well as the alleged bankrupt filed a special answer or motion to strike said petition for want of jurisdiction of the court to determine any rights in the fund. (Rec. 54-57.) The said National Builders Bank answered reserving the right to object to the entry of orders in any form other than by the agreement under which the funds were deposited. (Rec. 46.) The bankruptcy receiver claimed that the litigation of Odell was successful, and that the sum of $20,000 of the fund should be held until adjudication. (Rec. 51-53.) There was no further hearing on the said intervening petition, or the above-mentioned answers filed in opposition thereto.

On June 29, 1937, the intervening committee abandoned said petition and filed another petition in which they asked that $48,580.40 be turned over to them, exclusive of $20,000 of the fund over which there might be a dispute. (Rec. 69.) Appellants and the alleged bankrupt again objected on the ground that the court had no jurisdiction to determine the controversy. The question as to the jurisdiction was ordered referred to a Referee.

On the afternoon of the same day counsel for interveners presented a purported order which was signed by the court without the knowledge or consent of other counsel in the case which order purported to indicate that

the Court had directed appellants (petitioners here) to answer the petition, and each of them thereupon stated that they did not desire to answer said petition and further recited that they desired to stand upon the jurisdictional question theretofore raised. (Rec. 74.) This was not a fact or what occurred.

The petition and answers thereto raising the jurisdictional questions were referred to a referee, who on July 7, 1937 made his report. (Rec. 78.) The referee recommended that appellees' request be allowed, and that the sum of $48,580.40 be paid to the intervening committee, despite the fact that the reference to him and the issue before him were solely on the one question of jurisdiction. The court over objections allowed appellants two days to file exceptions to the report, in violation of rules granting 10 days, or 20 days if the referee was a special master. Appellants asked for an extension of time to file exceptions which leave was denied them. (Rec. 92.) Exceptions inadequately drawn were filed which called the attention of the court to the erroneous language in the order of reference, and the surreptitious manner in which it was obtained by counsel for interveners. (Rec. 92-5.) Appellants then asked leave to file an answer which would reply on the merits, which also was denied them. (Rec. 96.) Order was then summarily entered overruling exceptions and approving the referee's report and directing appellants to sign a check in favor of intervening alleged special committee for $48,580.40. (Rec. 96.) The next day the court granted appellees motion striking special jurisdictional answers theretofore filed by appellants. (Rec. 100.)

The District Court subsequently denied appellants leave to appeal. Appeal was later granted by the Circuit Court of Appeals. That court affirmed the orders of the District Court.

QUESTIONS PRESENTED.

1. Has a court of bankruptcy, prior to adjudication, jurisdiction to determine a controversy between escrowees of a fund, and certain beneficiaries of that fund (strangers to the proceeding) where the bankrupt has no interest in the controversy and neither appellant nor appellee are parties to the bankruptcy proceeding, and can such jurisdiction be conferred by consent?

2. Where a party has pleaded unsuccessfully to the jurisdiction, is he thereby precluded from pleading to the merits so that a court in denying such right may make a final determination on the merits, without trial, from factual information incidentally appearing in the pleadings?

3. Where the disbursement of a portion of funds in litigation is admittedly to the advantage of all parties, and such disbursement can be affected only by an agreed order, does participation in such agreed order constitute consent to the jurisdiction of the court, especially where the jurisdiction has theretofore been unequivocally challenged, and where the order allows an answer or other pleadings, and the subsequent pleadings further deny the jurisdiction of the court?

4. Is a fund in *custodia legis* for the purpose of conferring summary jurisdiction upon the bankruptcy court where it is subject to the joint order of three persons: (1) an officer of a corporation against which an involuntary petition in bankruptcy has been filed, (2) an attorney engaged to represent individual clients through the partial instrumentality of such corporation, and (3) the secretary of various trade associations of which the clients are members who is admittedly not connected with bankrupt?

5. Does the fact that funds are "closely connected" with the affairs of an alleged bankrupt, but control of which funds is not shown, place the funds in *custodia legis* and permit a summary distribution of the funds prior to adjudication?

6. Do any one or more of the following rulings of the trial court constitute an abuse of discretion tantamount to errors of law?

A. Disregarding equity and bankruptcy rules respecting time to file exceptions to referee's report.

B. Refusing an extension of time to file exceptions to referee's report.

C. Hearing collateral issues in bankruptcy prior to adjudication.

D. Permitting counsel for appellees in absence of other counsel to present draft order of reference misrepresenting facts of what occurred.

E. Taking jurisdiction over a fund concerning which an injunction of a state court was in effect.

7. Is an alleged bankrupt, a taxpayers association organized under Illinois law "not for pecuniary profit", such a "moneyed, business or commercial corporation" within the Act as to give the bankruptcy court jurisdiction for any purpose?

REASONS FOR GRANTING THE WRIT.

1. There is no provision in the Bankruptcy Act granting the District Court general jurisdiction to determine controversies between two third parties where the dispute does not involve the bankruptcy estate and in which it has no interest. The Bankruptcy Court transcended its jurisdiction in opening the door to miscellaneous litigation thus abolishing statutory limitations of the Bankruptcy Act.

2. The decision of the Circuit Court of Appeals that the bankruptcy court had jurisdiction of the controversy between appellants and appellees, (third parties) is in conflict with a much followed decision of the Circuit Court of Appeals for the Eighth Circuit, in the case of *Nixon* v. *Michaels*, 38 Fed. (2d) 420, holding that a bankruptcy court has no such jurisdiction and that jurisdiction cannot be conferred by consent. Decision at bar is also in conflict with decision in the Fourth Circuit in *Henrie* v. *Henderson*, 145 Fed. 316. The jurisdiction of the Bankruptcy Court to determine controversies where, as here, neither appellant nor appellee are parties to the bankruptcy suit, presents an important question of Federal Law which frequently arises in bankruptcy cases, and which has not been but should be determined by this court.

3. This court has never decided whether the phrase in the Bankruptcy Act: " * * * moneyed, business, or commercial corporation, * * * " (Title 11, Chap. 3, Sec. 22, (b) U. S. C. A.) confers jurisdiction to enter an involuntary adjudication over a corporation organized "not for pecuniary profit," such as a taxpayers association, or to settle collateral issues.

4. This court has never determined whether Sec. 23 of the Bankruptcy Act (Title 11, Chap. 4, Sec. 46, U. S. C. A.) relating to suits by trustees, upon consent of defendant, can be applied to confer jurisdiction over petitions of third parties to decide collateral issues foreign to the bankruptcy proceedings prior to adjudication and before appointment of a trustee.

5. This court has never decided whether disputed escrow funds not claimed by bankrupt estate are in *custodia legis* so as to give the court summary jurisdiction. The Seventh Circuit is in conflict with the Second Circuit

in this particular in *Buss* v. *Long Island Storage Warehouse* (64 Fed. (2d) 338) where summary jurisdiction was denied because the property was not unconditionally subject to the bankrupt's orders.

6. There was a departure by the trial court, sanctioned by the Circuit Court of Appeals, from the accepted and usual course of judicial proceedings in disregarding equity and bankruptcy rules, by denying sufficient time to file exceptions, by denial of leave to answer on the merits, by hearing collateral questions prematurely, by permitting counsel for appellees to present an erroneous draft order for signature in the absence of other counsel, by overruling valid exceptions to the referee's report and by the Circuit Court of Appeals determining questions on the merits without trial or hearing, all of which call for an exercise of this court's power of supervision.

7. The decision of the Circuit Court of Appeals that appellant Odell in acting as attorney for some of appellees, was an agent of the alleged bankrupt corporation, which was instrumental in his engagement, presents an important question of general law of particular interest. The finding is untenable with the weight of authority. Further, it presents an important question of Federal Law, with respect to jurisdiction of the bankruptcy court over property in the hands of an attorney for third parties,—questions which have never been decided by this court, and which should be so decided. Therein is also presented a departure from the accepted and usual course of judicial proceeding by the determining of said issues in the absence of answer or hearing thereon.

8. The Circuit Court in sanctioning the injection of a collateral controversy in the bankruptcy proceeding over which the bankrupt estate had no interest, conflicts

with the decision of the Supreme Court in the case of *Fulton Bank* v. *Hozier*, 267 U. S. 276, 280.

9. The decision of the Circuit Court of Appeals in making a finding upon issues raised by non-appealing parties, where the trial upon the merits of said issues had been postponed until the further order of the trial court, presents a question of general law probably in conflict with the weight of authority and constitutes a departure from the usual and ordinary procedure such as to call for the exercise of the powers of revision by this court.

10. The decision of the Circuit Court held that the court acquired jurisdiction over a fund closely connected with the affairs of the alleged bankrupt, even though the bankrupt had no interest in it and the record did not show control thereof by agents of the bankrupt. This presents an important question of Federal Law upon which this court has not, but should, decide. The extent of the jurisdiction of bankruptcy courts over property closely connected with the affairs of the bankrupt but not strictly bankrupt property, is an important question which frequently arises in the administration of bankruptcy estates. The present decision of the Circuit Court departs from the usual and customary practice of courts in bankruptcy matters.

11. In determining there was jurisdiction, the Circuit Court of Appeals overlooked these vital points: The case at bar concerned a controversy between strangers to the bankruptcy on a subject matter admittedly not a part of the bankruptcy estate. It is on these identical conditions that the generally followed Nixon case (38 Fed. (2d) 420) was decided. The decision in the case at bar is in conflict with the Nixon case and the weight of authority. Consent cannot confer jurisdiction over the subject mat-

ter. In this respect the Circuit Court of Appeals of this circuit is in conflict with decisions of the Supreme Court and the weight of authority as follows:

Mitchell v. *Mawrer*, 293 U. S. 237, 244.
Flanders v. *Coleman*, 250 U. S. 223, 228.
Hancock v. *Holbrook*, 112 U. S. 229, 231.
Railway v. *Swan*, 111 U. S. 379, 382-4.

Wherefore, it is respectfully submitted that this petition should be granted.

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KENART M. RAHN,
Attorneys for Petitioners.

BRIEF IN SUPPORT OF PETITION.

Opinions Below.

The orders of the District Court of the United States for the Northern District of Illinois, Eastern Division (Rec. 96, 99) have not been reported.

The opinion (Rec. 129) of the Circuit Court of Appeals has been reported in 95 Fed. (2d) 373.

Jurisdiction.

The orders appealed from, of the District Court, aforesaid, were entered July 12th and 13th, 1937, respectively (Rec. 96, 99). Appeal was denied in the District Court but was allowed by the Circuit Court of Appeals for the Seventh Circuit September 11, 1937.

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (C229, Sec. 1-43, Stat., 938, 28 U. S. C. A. Sec. 347 (a)), also under Rule 38 of this Court. The date of the judgment to be reviewed is March 9, 1938 (Rec. 129). Petition for rehearing was denied April 14, 1938 (Rec. 197).

Statement of the Case.

The material facts and the questions involved are set forth in the foregoing petition.

Specifications of Errors.

The Circuit Court of Appeals erred:

1. In permitting the bankruptcy court to assume jurisdiction over funds and controversies not involved in the bankruptcy estate.

2. In permitting the bankruptcy court to assume jurisdiction over a fund in litigation which was not in the control or custody of the alleged bankrupt or of the court.

3. In holding that jurisdiction over the subject matter was conferred by consent, or could be conferred by consent.

4. In permitting the bankruptcy court to entertain an intervening petition foreign to the bankruptcy proceeding.

5. In permitting the trial court to try collateral issues prior to determination of jurisdiction over the alleged bankrupt.

6. In not dismissing the controversy because of lack of jurisdiction over the alleged bankrupt.

7. In sanctioning the action of the trial court which arbitrarily restricted the time for the filing of exceptions to the referee's report, and refusing an extension thereof, all in violation of rules.

8. In sanctioning the action of the trial court in not dismissing the controversy as required by statute when lack of jurisdiction was called to its attention.

9. In sanctioning the arbitrary denial by the trial court of petitioners' right to plead to the merits, after a plea to the jurisdiction was decided unfavorably to them.

10. In finding that appellant was an agent of the alleged bankrupt when he was the attorney for contractors and hired by them.

11. In finding that the litigation with respect to the Illinois Sales Tax was unsuccessful when that issue was pending unheard, undetermined upon pleading of non-appealing parties in the court below, and the contrary was true in fact.

12. In finding that appellants neglected or refused to plead to the merits when the record shows they asked for and were denied opportunity to so plead after the overruling of their jurisdictional pleas.

13. In making findings of fact with respect to the balance of the fund, an issue which is not the subject matter of this appeal.

14. In finding that the escrow fund was closely connected with the affair of the alleged bankrupt, or was under the control of the alleged bankrupt and was, therefore, in *custodia legis*.

15. In taking jurisdiction over disputed funds involved in pending injunction in state court.

ARGUMENT.

Summary of Argument.

Point I — Court lacked jurisdiction to enter orders complained of and its decision is in conflict with other jurisdictions:

Controversy was between strangers to bankruptcy proceeding.

Funds in litigation not in custody of court or control of bankrupt and not bankruptcy assets.

Jurisdiction could not be and was not conferred.

Point II — The Court departed from the usual course of judicial procedure:

In denying hearing on the merits.

In disregarding rules of court.

Point III — The Court erred:

In hearing collateral matter when it had no jurisdiction over bankrupt.

In making findings of fact without a hearing.

ARGUMENT.

I.

The court of bankruptcy did not have jurisdiction to enter the orders appealed from.

The decision below is in conflict with the weight of authority and decisions of other circuits as well as decisions of the Supreme Court.

The general principle herein applicable with respect to jurisdiction is clearly enunciated in Remington on Bankruptcy, Fourth Edition (1936), Vol. V, Par. 2191:

> "Nor may third parties resort to the bankruptcy court to litigate their rights there, where neither the bankruptcy court has custody of the property, nor either of the parties was a party to the proceedings in bankruptcy, nor any property is recoverable by general creditors."

Neither these petitioners nor respondents here were parties to the bankruptcy proceeding. Omitting irrelevant details the facts are these: Four alleged bankrupt creditors filed an involuntary petition against a corporation. The corporation contended in good faith that it was not bankrupt. An alleged committee of three claiming to represent some two hundred odd individuals, utter strangers to the bankruptcy proceedings, sought to intervene. Their sole object in intervening was to obtain funds theretofore deposited with three escrow officers or trustees for a purpose which had no connection with the bankruptcy proceeding. The escrowees from whom they sought to obtain the funds likewise were strangers to the bankruptcy proceeding.

In the much followed case of *Nixon* v. *Michaels*, 38 Fed. (2d) 420 (8th Circuit followed in several circuits) a case in which an intervening petitioner attempted to have the bankruptcy court direct the holder of a check—proceeds of sale of bankruptcy assets—turn same over to petitioner, the court in holding that the bankruptcy court had no jurisdiction (a question raised for first time on appeal) said, on page 423:

> "But, leaving out of consideration preferential and fraudulent transfers, unless there is involved a *res* in the possession of the bankruptcy court and in which *res* as a part of the bankrupt estate third parties claim rights, the bankruptcy court has no jurisdiction to allow such third parties to come into the bankruptcy court merely to litigate therein rights even against parties to the bankruptcy proceeding, and even though the property involved may once have been part of the bankrupt estate. Remington on Bankruptcy (3d Ed.), Paragraphs 2191, 2199; *Henrie* v. *Henderson, supra; in re Hollins, supra; in re Girard Glazed Kid Co.* (D. C.), 136 F. 511; *in re Swofford Bros. Dry Goods Co.* (D. C.), 180 F. 549, 557; *in re Siegel* (C. C. A.), 256 F. 226."

Again in the case of *Henrie* v. *Henderson*, 145 Fed. 316, at 320, (4th Circuit) where a somewhat similar situation arose:

> "The object of the bankruptcy law is to afford the means by which the creditors of the bankrupt may secure an equitable and fair distribution of the bankrupt's property, etc., and the act contemplates that any collateral questions growing out of the settlement of the bankrupt's estate may be heard and determined in that court. But here we have parties who are contending about a matter which is in no way related to or connected with the affairs of the bankrupt. Under these circumstances, we fail to understand the theory on which this proceeding was instituted."

The alleged bankrupt corporation in case at bar at the time the involuntary petition was filed clearly had no custody or control of the funds.

The interveners themselves admit the absence of any connecting link between the estate of the alleged bankrupt and the fund in litigation in the following language:

> "all of the moneys deposited by the petitioners in said account in the National Builders Bank of Chicago, known as the Sales Tax Escrow Fund, were at the time of their deposit and at all times since, and are now solely the moneys of the petitioners, in which moneys neither the Tax Service Association of Illinois, William L. O'Connell, Jr., Receiver of said Tax Service Association of Illinois * * * have any right or interest * * *." (Rec. 28.)

The Sales Tax Escrow Fund was something set up entirely separate and apart from the Tax Service Association. Neither E. M. Craig nor Benjamin F. J. Odell were representatives of the Tax Service Association. Roy G. Harris, although a vice-president of the Tax Service Association, at the time the alleged agreement was entered into, acted in his own individual capacity and not as a representative or officer. The funds in question were deposited in the National Builders Bank of Chicago in a special fund entitled Sales Tax Escrow Fund. Checks were made out directly to this Sales Tax Escrow Fund by the contractors. Funds could be released from this escrow only upon the written order of all three escrowees acting jointly. The interveners alleged (Rec. 28) that in the escrow matter Craig was acting as representative of the interveners and of various building associations of which the interveners were members. Craig was the secretary of the Building Construction Employers' Association of Chicago, a master association comprising the said mentioned associations. It has nowhere been even sug-

gested that he was acting for or in any sense subject to the control of the Tax Service Association. In view of Craig's admitted independence of the Tax Service Association, and of the absolute necessity of his concurrence in order to withdraw any funds from the escrow, any contention that the said fund was in the custody or control of the alleged bankrupt corporation would be patently absurd. He was selected by the contractors as positive assurance against even possible interference, domination or control of the funds by the alleged bankrupt.

The Court misconstrued the law and the facts in intimating that the funds were in the possession of the bankruptcy court. In order to be *custodia legis*, the rule is well settled, property must be in the possession of an officer of the court or must be deposited in court.

Possession becomes material only when there is a dispute between a trustee and an adverse claimant, over the *estate of the bankrupt*. The Bankruptcy Act grants jurisdiction as follows:

> "(7) Cause the estate of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided." U. S. C. A. Title 11, Chap. 2, Sec. 11.

Clearly jurisdiction to determine controversies must relate to the *estate of the bankrupt*.

This section has two requirements: First, the controversy must relate to the estate, and second, there must be a bankrupt—*i. e.*, there must be an adjudication. In the case at bar, neither element was present. The controversy does not relate to the estate of the bankrupt, because the $48,500 is not and never has been claimed by the bankrupt, or the receiver. There was no bankrupt—there had been no adjudication.

The decision of the Circuit Court is in conflict with a decision of the Supreme Court in the case of *Fulton Bank* v. *Hozier*, 267 U. S. 276 at 280 and 281. In that case an intervener sought to have the bankruptcy court recover property from a third person for his benefit. The Court said:

> "The general rule is that when a Federal Court has properly acquired jurisdiction over a cause it may entertain, by intervention, dependent or ancillary controversies; but no controversy can be regarded as dependent or ancillary unless it has a direct relation to property or assets actually or constructively drawn into the court's possession or control by the principal suit. • • •
>
> "He had no right to bring the bank, which for jurisdictional purposes was to be deemed a citizen of Georgia, Jud. Code (24, Subdiv. 16) into the Federal Court or to intervene with the affairs of the estate by injecting this controversy concerning which the receivers had no material interest—wherein the estate might lose much but could gain nothing."

There is no possession of the fund in controversy in the bankruptcy court. This fact cannot be disputed. The funds are in the National Builders Bank,—not in court. The bank has filed what might be termed a special and limited answer (Rec. 46) reserving rights to object to any distribution of funds other than by the agreement of deposit. The alleged bankrupt does not have them in its possession. The court's officers do not have possession of them.

Even if the court were correct in assuming that this was a controversy relating to the estate of the bankrupt, the decision of the Circuit Court is in conflict with the decision of the Circuit Court of the Second Circuit. In the case of *Buss* v. *Long Island Storage Warehouse*, 64 Fed. (2d) 338, 340, the bankruptcy court attempted to exercise summary jurisdiction over property in a warehouse.

The court there held that there was no summary jurisdiction, because the warehouseman was not unconditionally subject to the bankrupt's orders. The Court said on page 340:

> "* * * As we have said, the underlying notion is that for jurisdiction to attach, the bailee must be unconditionally subject to the bankrupt's orders * * *".

The alleged bankrupt could not exercise any domination over the fund, without the written concurrence of Craig, whom all agree had no connection whatever with the alleged bankrupt. The finding of the Circuit Court is directly in conflict with the Buss case, and there exists a confusion between the Circuits which this Court should clarify.

The law is well settled that jurisdiction of the subject matter cannot be conferred upon a court by consent.

In the early case of *Olds Wagon Co.* v. *Benedict*, 67 Fed. 1, 5 (C. C. A. 8, 1895), the court used language now universally concurred in:

> "* * * No consent agreement or estoppel can confer jurisdiction upon a federal court to determine any case in which the essential jurisdictional facts do not appear from the record. These rules are fundamental. They are settled by repeated adjudication of the Supreme Court, * * *".

In the case of *Nixon* v. *Michaels*, 38 Fed. (2d) 420, above discussed, the court used the following significant language on pages 422, 423:

> "(2) The question of jurisdiction was not raised directly in the court below; nevertheless, it is the duty of this court to determine the question. *M. C. & L. M. Ry.* v. *Swan*, 111 U. S. 379, * * *; *C. B. & Q. Ry. Co.* v. *Willard*, 220 U. S. 413, 419, * * *; *B. & O. R. Co.* v. *City of Parkersburg*, 268 U. S. 35,

* * *; *Highway Const. Co.* v. *McClelland*, 14 F. (2d) 406 (C. C. A. 8)."

"(3) A District Court of the United States sitting as a court of bankruptcy is a court of limited jurisdiction. Limitations exist as to subject matter; as to territory; as to the residence and occupation of the debtor to be adjudicated; as to the status of the corporation or person to be adjudicated; and as to other matters. Remington on Bankruptcy (3rd Ed.), c. III. And consent cannot confer jurisdiction over subject matter. The express provisions of the statute and the necessary implications are controlling. *Id.* p. 66; *Bardes* v. *Howarden Bank*, 178 U. S. 524, 535, * * *; *Henrie* v. *Henderson* (C. C. A.), 145 F. 316, 320; *Nelson* v. *Svea, etc., Co.* (D. C.), 178 F. 136, 140; *In re Hollins* (C. C. A.), 229 F. 349; *Id.* (C. C. A.), 238 F. 787; *Jones* v. *Kansas City, etc., Co.*, 1 F. (2d) 649 (C. C. A. 8); *In re Judith, etc., Co.* (C. C. A.), 5 F. (2d) 307."

The lower courts in this case are definitely in conflict with the Supreme Court on the question of conferring jurisdiction over the subject matter by consent of parties as the following authorities show:

Mitchell v. *Mawrer*, 293 U. S. 237, 244.
Flanders v. *Coleman*, 250 U. S. 223, 228.
Hancock v. *Holbrook*, 112 U. S. 229, 231.
Railway v. *Swan*, 111 U. S. 379, 382-4.

There was no consent to the jurisdiction. These petitioners did not confer jurisdiction on the court by consent if that were legally possible. The Circuit Court of Appeals was in error in finding such consent.

"* * * It was at the solicitation and suggestion of the court that said 75 per cent of the funds were distributed to the Department of Finance for the various petitioners in order to avoid a penalty against said petitioners for failure to pay said taxes within the allotted time, and it was stated by respondents and agreed to in open court that the consent requested by the court to such distribution would not

prejudice the rights of respondents to have determined the question of the jurisdiction of the court over the 25 per cent balance of said funds." (Exceptions to referee's report (Rec. 93-94).)

The first intervening petition was filed on May 24, 1937. June 1, 1937, was the "deadline" for the payment to the State Department of Finance of taxes from the escrow fund in order to avoid the imposition upon and accrual to the interveners of heavy penalties in excess of $100,000.

At the time of the entry of the order it was insisted by these petitioners and agreed in open court that the consent requested by the court to such distribution would not prejudice their rights to have determined the question of the jurisdiction of the court over the 25% balance of said fund. (Rec. 93-94, 62.) That the court so understood the agreement is evidenced by the fact that the order itself gave these petitioners the right to file "their answer *or other pleadings* to said petition (Avery Brundage or first petition), * * * to and including June 3, 1937." What is meant by "other pleadings"? Clearly the expression as herein used is broad enough to include, and was intended to include, pleas to the jurisdiction.

II.

The court erred in denying a hearing on the merits.

There is nothing special or peculiar about the Bankruptcy Act which deprives a defendant or respondent of his right to plead to the merits of a cause because he has first availed of his right to plead to the jurisdiction. A plea to the jurisdiction in any controversy does not sacrifice the right to subsequent pleadings on the merits. Indeed appellants were within their rights in so enlightening the court on this important jurisdictional question.

"If in any suit commenced in a District Court * * * it shall appear to the satisfaction of the said District Court at any time after such suit has been brought * * *, that such suit does not really and substantially involve a dispute or controversy property within the jurisdiction of said District Court, or that parties to said suit have been improperly or collusively made or joined, either as plaintiffs or defendants for the purpose of creating a case cognizable * * * under this chapter, the said District Court, shall proceed no further therein, but shall dismiss the suit * * *, as justice may require, and shall make such order as to costs, as shall be just." Title 28, Paragraph 80, United States Code.

Clearly it is not the intent of this act to deprive parties of a hearing on the merits. Because of this plea to the jurisdiction, appellants were deprived of their rights to go into the facts which were vital for the court to know before issuing a summary order disposing of the large amount involved in this cause. Had the court not arbitrarily denied the motion to file answer to the merits, it would have been informed on the facts showing: that the funds involved in the petition were subject to an attorney's lien, as Odell had not been paid for the services rendered the contractors for whom he had been eminently successful, (*Blome Co.* v. *Ames*, 365 Ill. 456, 459, and *Herlihy Mid-Continent Co.* v. *Nudelman*, 367 Ill. 600, 605); that intervener's petition was not actually the petition of all of the contractors; that a liability existed if appellants as escrow officers or trustees turned over the funds without special written request from each contractor or without an indemnity for so doing; that a definite deception was practiced upon these petitioners to procure their signature to the order of May 27th; that the contractors hired Odell by written contracts independent of the contract between trade associations and the alleged bankrupt, and that he is entitled to the wage of his hire; that there

was an acceptance of the services of Odell and there was an express agreement to pay him; that an injunction was issued in the State Court that had jurisdiction of the matter in Superior Court Case No. 37 C 1716 enjoining these petitioners from disbursing the said funds in escrow and said injunction is still in force and effect; that on May 12, 1937, a restraining order of the United States District Court in this very case was entered in effect preventing the dissolution of the said injunction in the State Court and that it is still in full force and effect; that the disbursing of said funds would be a violation of said injunctions; that there was no actual consent by appellants to the jurisdiction of the court; that appellants believe the intervening petitions were filed without authority and knowledge of many of the contractors. These and other important facts do not pass before the court for consideration upon a summary disposition of this cause on a mere jurisdictional plea, yet $48,580 involved was thus arbitrarily disposed of.

These petitioners are thus deprived of due process of law as secured to them by the United States Constitution in Article V of Amendments thereof. They have not been given their day in court to present their defense or be heard on the merits thereof.

The Court Abused Its Discretion in Disregarding the Equity and Bankruptcy Rules and Denying Sufficient Time to File Exceptions.

In the haste which characterized this entire proceeding, confusion and misunderstanding resulted between referee and court, and which, but for the gravity of the situation, might be characterized as a comedy of errors having the effect of depriving appellants of any hearing whatsoever upon the merits of the controversy.

The second intervening petition was filed June 29, 1937. (Rec. 69.) Appellants had already filed their special answers questioning the jurisdiction of the court and otherwise reserving all rights. (Rec. 54-55.) The court had previously ordered the filing of answers. (Rec. 41.) The special answers of appellants, previously filed to the jurisdiction, were permitted to stand to the second petition. (Rec. 74.) The latter petition, together with the special answers, were referred to the referee the same day they were filed, June 29, 1937. (Rec. 73-5.) That order of reference was limited to the sole question of jurisdiction. (Rec. 75.) Other issues then pending were not referred to the referee. (Rec. 46-53.) Notwithstanding the restriction on the referee to hear and report on the jurisdiction question only, he reported on the merits without having any hearing on the merits, and found allegations of the second petition true. (Rec. 78.)

In his report the referee referred to certain sections in the order of reference (Rec. 84, 85) in which it appears that the appellants were asked whether or not they desired to answer the second petition. The order recites appellants responded that they did not desire to answer said petition but asked that the special answer to the first petition stand to the second petition, and to which the court consented. The order is incorrect. The alleged statement by appellants that they wished to be heard first on the jurisdiction before answering to the merits should not be construed as depriving them of their right to be heard on the merits later.

The order of reference was obtained under most unusual circumstances. Sigmund W. David, attorney for the intervening petitioners, presented his order of reference to the court in the absence of all other counsel and without their approval, and copies of the draft order were

not given to other counsel until the day after it was entered. (Rec. 92.) That reference order falsely related that appellants had stated they did not desire to answer the petition. At no time did the appellants say they did not desire to answer the petition or be heard on the merits. To the contrary they sought hearing on the merits. (Rec. 96.)

On July 7, 1937, the referee's report was presented to the court recommending the signing of a check by your petitioners for some $48,580 and further recommending that the National Builders Bank of Chicago honor and pay the same despite the fact the matter had not been referred to the referee on the bank's answer and the bank had not been present at the hearing nor had there been any hearing on the merits concerning the bank's, or anyone else's answer.

The court on July 9, 1937 (Rec. 91), ordered appellants to file exceptions to the referee's report within two days. The court was requested at this time to allow them ten days as provided by Rule 14 of the Bankruptcy Act for the purpose of filing their exceptions to the referee's report. The trial court, however, took the position that the matter had been referred to the referee as a Special Master for the purpose of determining the issues in the petition. Thereupon appellants drew it to the court's attention that (for Master's reports) under Rule 66 for Courts of Equity of the United States, appellants should be allowed twenty days in which to file exceptions. (Rec. 95.) The trial court, however, insisted the matter should be summarily disposed of within three days and this, nowithstanding the fact that the hearing on the adjudication of the alleged bankrupt, over its strenuous objection, had been continued to the fall. On the coming into court on the 12th day of July, 1937, appellants again moved the

court for a sufficient length of time in which to file their exceptions to the Special Master's report, which motion the trial court denied. (Rec. 92.) Thereupon these appellants filed their exceptions to the report (Rec. 92), summarily and insufficiently prepared, in which, however, they briefly set forth the injustice done them in hurrying this matter and depriving them of a respectable hearing.

There was set forth in their exceptions that the order of reference dated June 29, 1937, stated erroneous facts and that the order was presented to the court in the absence of other counsel; that appellants were desirous of having their special answers to the jurisdiction disposed of before they answered to the merits and that appellants did not waive their right to plead to the merits; that the erroneous portion of said order had misled the Special Master, and as his report indicated, furnished the sole reason for his recommending that the prayer of the intervening petition be granted against appellants without appellants being given an opportunity to be heard on the merits. (Rec. 92.)

Those exceptions set forth many reasons why the Special Master's report should not be approved and the court's attention is respectfully directed to them on pages 92 to 95 of the Record.

The trial court sustained the Special Master's report, as erroneous as it was, and thereby denied appellants, not only their right to sufficient time to prepare and argue exceptions to the Special Report, but also deprived appellants of their right to be heard in court on the merits of the issues.

The District Court, and the Circuit Court of Appeals in affirming the District Court, have so far departed from the accepted and usual course of judicial proceedings or so far sanctioned such a departure as to call for an exercise of this court's power of supervision.

III.

Further errors of the Circuit Court of Appeals and the Trial Court.

NO JURISDICTION OVER ALLEGED BANKRUPT.

Both the trial and the reviewing court committed error in entertaining the intervening petition. The alleged bankrupt is a corporation organized "not for pecuniary profit" under the Laws of the State of Illinois, Smith-Hurd, Chapter 32, Sec. 158-163. (Rec. 6, 56, 77.)

A taxpayers association organized not for pecuniary profit, is not within the purview of the Bankruptcy Act:

> "* * * Any unincorporated company, and any moneyed business, or commercial corporation (except a municipal, railroad, insurance, or banking corporation, or a building and loan association) owing debts to the amount of $1,000 or over, may be adjudicated an involuntary bankrupt upon default or an impartial trial." Section (b) of Bankruptcy Act. (Title 11, Chapter 3, Section 22, U. S. C. A.)

The Court had no jurisdiction over the alleged bankrupt because the alleged bankrupt was not and cannot be subject to the Act. Of necessity, the court had no jurisdiction over collateral matters, either before or after adjudication. In this case, all the orders were entered prior to the adjudication. This question of jurisdiction may be attacked at any time by anybody.

Respondents may contend that an adjudication determines this issue, however, if the trial court has no jurisdiction over the subject matter, all orders, collateral or otherwise, are null and void and subject to collateral attack.

The Supreme Court has never determined the question of jurisdiction of Bankruptcy Courts over corporations

organized "not for pecuniary profit", and has never determined the power and authority of a Bankruptcy Court to entertain purely collateral matters prior to adjudication. These questions should be decided by this court.

Disregard of Rules.

The trial court erred in disregarding Equity Rule 66, applicable here because the referee sat as a special master:

> "The master, as soon as his report is ready, shall return the same into the clerk's office, and the day of the return shall be entered by the clerk in the equity docket. The parties *shall have* 20 days from the time of the report to file exceptions thereto, and if no exceptions are within that period filed by either party, the report shall stand confirmed. If exceptions are filed, they shall stand for hearing before the court, if then in session, or, if not, at the next sitting held thereafter, by adjournment or otherwise."

The arbitrary restriction of time in which to file exceptions to the report of the referee, and the flat refusal of a motion for an extension of time (Rec. 92) when taken in connection with the other errors in this case, constitutes a departure from the usual and ordinary standard of judicial procedure as to call for an exercise by this court of its powers of supervision. Do the court rules apply only to litigants and not to the courts?

Approval of Untrue Orders.

The sanction by the Circuit Court of Appeals of the trial court's error in permitting counsel for appellees to present an untrue order for signature without the knowledge of other counsel, and the subsequent overruling of appellants exceptions which called attention to the injury and imposition (Rec. 92) are a departure from the usual

and accepted standards of judicial procedure, and when taken in consideration with the other errors of the trial court, calls for the exercise by this court of its powers of supervision.

Findings of Fact Without Trial.

The departure by the Circuit Court from its usual procedure by making findings of fact upon issues not before the court, calls for the exercise by this court of its powers of supervision. For example, the Circuit Court of Appeals purported to find that Odell was unsuccessful in the litigation with reference to the Sales Tax. That issue was not before the Circuit Court of Appeals and was never tried in either court although pending undisposed of in the District Court on pleadings of non-appealing parties. The Illinois reports heretofore cited show Odell was eminently successful in the tax case. Again the court erred in finding that appellants neglected or refused to answer to the merits. They had asked for an opportunity to plead to the merits on July 12, 1937, prior to the entry of the order appealed from. (Rec. 96.) The Court arbitrarily denied that motion. The appeal was from that and other orders.

The Circuit Court of Appeals erred in finding that Odell, in acting as attorney for the contractors, was an agent of the alleged bankrupt. (Rec. 132.) Each of the contractors had separately engaged Odell to represent them, and appendix *infra* is an example of one of the forms of engagement. The Tax Service Association was not a party to the sales tax litigation. The contractors brought suit in their own names in the Circuit Court of Cook County and the Supreme Court of Illinois. Odell was their attorney. He was clearly the agent of the contractors, not of the alleged bankrupt.

The Circuit Court of Appeals erred in making findings of fact when the lower court had denied pleading on the merits and hearing on the facts. This was a departure from the usual and accepted judicial procedure such as to call for supervision by this court. This method of procedure is contrary to the weight of authority.

CONCLUSION.

Because this case involves conflicts with the United States Constitution, with the United States Statutes, with decisions of the United States Supreme Court, with decisions of other circuits and because the lower courts departed from the usual course of judicial proceedings, it is urged that the writ of certiorari, as herein prayed, be granted.

Respectfully submitted,

BENJAMIN F. J. ODELL,
KENART M. RAHN,
Attorneys for Petitioners.

APPENDIX.

Example of form of employment of attorney Odell used by some of the contractors:

"On the recommendation of The Builders Association, we hereby consent to the employment of Benj. F. J. Odell as our attorney to represent us in negotiations and litigation in an effort to change the present ruling of the Retailers' Occupation Tax Act as it applies to us, the expense in no event to exceed three months' savings of such taxes, payment of our share of the expenses to be made with the approval of The Builders Association under their agreement with said Odell as to a gross maximum fee. The above is subject to Bulletins issued by Mr. Craig dated April 17th and 23rd, 1935.

DAHL-STEDMAN CO.
GEO. V. DAHL
(SEAL) *As President.*

DAHL-STEDMAN CO.
ELMORE W. STEDMAN
April 25, 1935 *As Sec'y & Treas."*
(Rec. 169-170)

The material provisions of the bankruptcy act, with reference to jurisdiction of the District Court, are as follows:

"(7) Cause the estate of bankrupt to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as otherwise provided * * *"

(Title 11, Chapter 2, Section 11, U. S. C. A.)

"(a) The United States District Court shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy, between trustees as such and adverse claimants concerning the property acquired or claimed by the trus-

tees in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupt and such adverse claimants.

(b) Suits by the trustee shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted, unless by consent of the proposed defendant, except suits for the recovery of property under section 96, subdivision b of this title; section 107, subdivision e of this title; and section 110, subdivision e, of this title."

(Title 11, Chapter 4, Sec. 46, U. S. C. A.)

"(b) Any natural person, except a wage earner or a person engaged chiefly in farming or the tillage of the soil, any unincorporated company, and any moneyed, business or commercial corporation, except a municipal, railroad, insurance, or banking corporation, owing debts to the amount of $1,000 or over, may be adjudged an involuntary bankrupt upon default or on impartial trial, and shall be subject to the provisions and entitled to the benefits of this title."

(Title 11, Chapter 3, Section 22, U. S. C. A.)